

MONGOLIA

RESOLUTION OF THE FINANCIAL REGULATORY COMMISSION

January 29, 2014

ref no 37

Ulaanbaatar

To authorise the approval of “Regulation on Licensing and undertaking Custodian’s activities”

According to Article 6.1.2 of Law on the Legal Status of Financial Regulatory Commission, Article 34.1.3 of Securities Market Law, and Article 15.3.5 of Law on Licensing, Financial Regulatory Commission hereby RESOLVES:

1. As stated in article 46.2 of Securities Market Law, since the Financial Regulatory Commission and Mongolbank legalised to jointly approve the regulation on licensing and undertaking Custodian’s activities, Financial Regulatory Commission /D.Bayarsakhan/ is hereby authorized to approve the draft regulation as set in appendix by the joint resolution of President of Mongolbank.
2. To endorse the Working Group /Kh.Bum-Erdene/ to arrange following activities such as to implement this newtype of service in the Securities Market as according to legislations, international common principles and national features, to develop substructure, to advertise it as accessible to market professionals and investors as specified in the plan in appendix.

CHAIRMAN

D. BAYARSAIKHAN

JOINT RESOLUTION  
CHAIRMAN OF FINANCIAL REGULATORY COMMISSION  
And  
GOVERNOR OF MONGOLBANK

July 3<sup>rd</sup>, 2014

ref no 85/A-106

Ulaanbaatar

Approving the regulation on custodian licensing and operation

Based on the article 46.5 of Securities Market Law, it is hereby ORDERED:

1. To approve the regulation on licensing and undertaking Custodian's activities as set in the Appendix.
2. To assign Supervision Department, Mongolbank /D. Ganbat/ to set the revised percent of operational risk fund of custodian at the end of each year.
3. To endorse the Supervision Department, Mongolbank /D. Ganbat/ and Securities Department, Financial Regulatory Commission /T.Jambaajamts/ to monitor the implementation of the approved regulation.

CHAIRMAN OF  
FINANCIAL REGULATORY COMMISSION

GOVERNOR OF  
MONGOLBANK

D.BAYARSAIKHAN

N.ZOLJARGAL

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## **REGULATION ON CUSTODIAN LICENSING AND CUSTODIAN SERVICES**

### **One. General Provisions**

- 1.1. The objective of this Regulation is to define the rules for the issuance, suspension, renewal and revocation of a license to operate Custodian Services as granted by the Financial Regulatory Commission (the "Commission") and to regulate the terms and requirements for Custodian Services and other regulatory matters related to them.
- 1.2. A Custodian shall abide by the relevant provisions of the Civil Law, the Company Law, the Banking Law, the Securities Markets Law, the Investment Fund Law, the Law of Mongolia on Combatting Money Laundering and Terrorism Financing and other relevant legislation and regulations issued by the Commission and other relevant authorities.
- 1.3. Only a [legal] person specified in Article 46.2 of the Securities Markets Law shall be entitled to act as a Custodian.
- 1.4. The Commission and the Bank of Mongolia (the "BoM") shall only grant a license to act as a Custodian to [legal] persons that meet the requirements as stated in the Securities Markets Law, the Banking Law, the Investment Fund Law as well as this Regulation.
- 1.5. In addition to this Regulation, the Commission and/or the BoM have the power to approve and issue further rules and regulations with respect of Custodian Services on its/their own or jointly with other relevant authorities.
- 1.6. The following terms used in this Regulation shall have the meanings ascribed to them as follows:
  - 1.6.1. "Custodian Services" mean the [regulated] activities referred to in Art.46.1 of the Securities Markets Law;
  - 1.6.2. "Securities" mean the financial instruments referred to in Art. 5.1 of the Securities Markets Law;
  - 1.6.3. "Nominal Owner" (or "Nominee") means the [legal] person referred to in Art. 4.1.25 of the Securities Markets Law;
  - 1.6.4. "Beneficial Owner" means the person referred to in Art. 4.1.26 of the Securities Markets Law;
  - 1.6.5. "Collective Account" means an account opened with Central Securities Depository and operated by a Custodian on behalf of one or more Beneficial Owners;
  - 1.6.6. "Investor" means an individual or a legal person that has purchased a financial instrument traded on a regulated market or over-the-counter;
  - 1.6.7. "Custody Operations Unit" mean the [separate] department, division, section or its equivalent within the [organizational] structure of a Custodian which performs Custodian Services;

- 1.6.8. “Corporate actions” mean events in the life of a listed company that occur upon the decision by authorized bodies of that company and that directly impact its shares and/or its shareholders and bondholders (as further defined in Section 3.13 of this Regulation);
- 1.6.9. "Business Day" means a day other than those set out in Articles 76.1 and 77.1 of Labor Law of Mongolia or any Monday, Tuesday, Wednesday, Thursday and Friday.

## **Two. Issuing a license to provide custodian services**

- 2.1. The Commission shall issue a license to provide custodian services to a bank or its controlled company or subsidiary<sup>1</sup> or to Central Securities Depository (the “CSD”) as set out in Article 46.2 of the Securities Markets Law and which meet the requirements as stated in the law and this Regulation.
- 2.2. To qualify for a license, an applicant must satisfy the following conditions and requirements:
- 2.2.1. The applicant must be incorporated in accordance with the applicable laws [of Mongolia] and registered in the State Registry of Legal Entities;
- 2.2.2. If the applicant is a bank, it must have the amount of paid-in capital required for banks by the BoM; if the applicant is a person other than a bank, the exact capital requirements [for a custodian] shall be determined by the Commission;
- 2.2.3. The applicant must meet the requirements as described in Article 8 of this Regulation;
- 2.2.4. The applicant must meet the requirements set out in Article 9 of this Regulation, must employ not less than 6 (six) people who hold the license [granted to it by the Commission] to operate in the securities markets and who have no less than 3 years of the appropriate experience in the banking, finance or capital markets sector;
- 2.2.5. Governing persons<sup>2</sup> and other staff of the applicant shall meet the following requirements:
- 2.2.5.1. have ethical and business integrity consistent with his/her role of managing the applicant;
- 2.2.5.2. have no record of conviction in any anti-state, economic or terrorism financing crimes;

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<sup>1</sup> Translator’s note: A “*subsidiary*” is defined as an entity in which another (parent) company owns 20% - 50% of all the common shares, a “*controlled company*” is defined as an entity in which another (parent) company holds more than 50% of common shares. (Art. 6 of the Company Law).

<sup>2</sup> Translator’s note: A “governing person” under Mongolian Company Law is defined as “A person who participates directly or indirectly in the process of making official decisions of a company or concluding transactions or agreements, such as members of a Board of Directors and executive management team of a company, the executive director, chief financial officer, chief accountant, chief officer, secretary of Board of Directors shall be deemed to be governing persons of the company.” (Art. 84.1)

- 2.2.5.3. have no role of a governing person in other professional participants of the financial markets.
- 2.2.6. If the applicant is a bank's controlled company or subsidiary, then it [applicant] must have at least 3 board members, of which at least one must be independent member;
- 2.2.7. Staff employed in a Custody Operations Unit must obtain a license to operate [as a professional] in the securities markets in accordance with the procedure set out in Art.35 of the Securities Markets Law;
- 2.2.8. Staff who directly perform the custodian services must have professional indemnity insurance as described in Section 9.9 of this Regulation;
- 2.2.9. The applicant must operate and maintain a web site to disclose relevant information to the public;
- 2.2.10. The applicant must ensure the reliability of its equipment, technology and software to exchange information and process transactions with the BoM, Mongolian Stock Exchange (the "MSE"), the CSD, other professional market participants and clients as described in Article 8 of this Regulation;
- 2.2.11. The applicant must procure a confirmation from relevant authority in respect of its compliance with requirements of the BoM, the MSE and the CSD in respect of proper communications and information exchange;
- 2.2.12. The applicant must have a system to store and restore the necessary information on client accounts and holdings, financial instruments held and any other relevant information in case of errors or failure of a network or software as described in Article 8 of this Regulation;
- 2.2.13. The applicant must pay the state stamp duty and regulatory service fee, as fixed by law or by the Commission;
- 2.2.14. Any other applicable requirements specified by the Commission and/or the BoM.
- 2.3. If the applicant is a bank, such applicant shall satisfy the following additional requirements in addition to those specified in Section 2.2 of this Regulation:
  - 2.3.1. The applicant must have a separate and independent Custody Operations Unit;
  - 2.3.2. The Custody Operations Unit, its governing persons and other staff [of the Unit] shall have no other position or role of a different type within the applicant bank;
  - 2.3.3. The Custody Operations Unit shall possess an adequate infrastructure for providing clients with custodian services per the requirements as described in Article 8 of this Regulation;
  - 2.3.4. Financial records, accounts, reports, records of official documents and any confidential information of the Custody Operations Unit shall be kept separate from those of the applicant's [bank's] other documents and operations and shall be accessible only for the staff working in the Custody Operations Unit;
  - 2.3.5. The accounting of custodian services must be performed and stored in accordance with the regulations and standards issued by the Commission and the CSD, which shall be consistent with international accounting standards. Template financial

- statement consistent with international accounting standards shall be delivered to the Commission;
- 2.3.6. The databases and other machine-readable information, all hardware and software of the Custody Operations Unit must meet the requirements as described in Article 8 of this Regulation and shall be accessible only to the authorised staff working in the Custody Operations Unit;
- 2.3.7. The applicant [the bank] must have obtained a banking license from the BoM at least 3 years [prior to applying for a license as custodian];
- 2.3.8. The shareholders, chairman or the members of the board, executive management as well as other governing persons of the applicant [bank] must meet the requirements set out by the relevant paragraphs of the Banking Law and meet the requirements of a “fit and proper person” set out by the relevant paragraphs of the Securities Markets Law.
- 2.4. All applicants must submit the following documents and materials in addition to those specified in the paragraph 11.1 of the Law on Licensing Business Activities, paragraph 27.2 of the Securities Markets Law and paragraph 6.3 of the Banking Law:
- 2.4.1. A notarised copy of the state registration certificate;
- 2.4.2. A document identifying affiliated persons/related persons<sup>3</sup> and information about them;
- 2.4.3. The following information with respect to the chairmen and members of the board and of the audit committee as well as the executive management team:
- 2.4.3.1. Curricula vitae;
- 2.4.3.2. [Independent] statements on the existence (or absence) of outstanding taxes owed or overdue loans from banks or non-bank financial institutions, [independent] statements on the existence (or absence) of pending payments or debts under any court rulings or judgements;
- 2.4.3.3. The Commission shall procure the statements set out in Section 2.4.3.2 of this Regulation from the police or from the credit information database in accordance with law.
- 2.4.4. Internal policies and procedures for the custodian services in respect of the following matters:
- 2.4.4.1. The use, maintenance and protection of client information, documents and materials;
- 2.4.4.2. The delivery of information concerning custodian services to clients;
- 2.4.4.3. The code of conduct for the management and employees;
- 2.4.4.4. Identifying, detecting, preventing and reporting conflicts of interest;
- 2.4.4.5. Prevention and management of external events, including problems caused by force majeure and man-made disasters;

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<sup>3</sup> Translator’s note: For definition of an “affiliated person”, please see Art. 999 of the Mongolian Company Law. For definition of a “related person” to bank, please see Art. 3.1.2 of the Mongolian Banking Law

- 2.4.4.6. Prevention of economic [money laundering] and terrorist financing crimes;
- 2.4.4.7. Prevention of market abuse;
- 2.4.4.8. Notarised copies of property certificates, if the Custody Operations Unit is located on the applicant's own property, or a notarised copies of lease if the premise is rented.
- 2.4.5. Audited financial statements of the applicant for the last 3 (three) financial years; the auditor that audited the aforementioned documents must be registered with the FRC or must be an internationally recognized firm;
- 2.4.6. Risk management policy that meets the requirements as described in Article 10 of this Regulation;
- 2.4.7. Technical description of the applicant's hardware and software per the requirements described in Article 8 of this Regulation;
- 2.4.8. Curricula vitae of the governing persons and personnel of the Custody Operations Unit in the form of the attachment [to this Regulation];
- 2.4.9. A no objection letter from the Governor of the BoM to [the applicant's] provision of custodian services as described in paragraph 6.4 of the Banking law;
- 2.4.10. Other documents as reasonably required by the Commission.
- 2.5. A license for custodian services shall be issued for an indefinite term, but it may be suspended or revoked by the Commission in accordance with Article 13 of this Regulation.
- 2.6. The Commission shall review the application for a license and relevant [accompanying] documents and make a decision within 30 (thirty) calendar days from receipt of the complete application.
- 2.7. If additional investigation and clarification is needed, the Commission shall make a decision within 20 (twenty) calendar days after receiving additional [requested] information from the applicant.
- 2.8. In the following circumstances, the documents submitted by an applicant shall be returned to the applicant [by the Commission] within 20 (twenty) calendar days:
  - 2.8.1. The documents submitted [by the applicant] for a license do not fulfil the requirements in the relevant laws and in this Regulation;
  - 2.8.2. The application for a license does not satisfy the requirements and conditions of licensing described Sections 2.2 and 2.3 of this Regulation;
  - 2.8.3. It was determined that the applicant submitted or used fraudulent documents;
  - 2.8.4. Application was filed with the Commission within 1 year after the previous license was revoked pursuant to Section 2.8.3 of this Regulation or the application was rejected within the last year;
  - 2.8.5. Other cases specified in the laws or regulations or defined by the Commission.
- 2.9. Application for a license shall be returned to the applicant pursuant to Section 2.8 of this Regulation along with a reasonable explanation in writing.



- 2.10. If the Commission has refused to issue a license on the grounds of fraudulent documents, the Commission shall not accept an application from a legal entity which is an affiliated person/related party with a shareholder, board chairman or member, or executive management of the applicant within 1 year since the statement of refusal was delivered to the applicant.
- 2.11. If the applicant has been issued by the Commission a License, the license shall be registered in the unified registry of licenses pursuant to a relevant regulation.

### **Three. Functions and types of activities of a custodian**

- 3.1 Custodian services shall comprise providing custody for the securities owned by client and conducting other services related to exercising other ownership rights as defined in Article 46.1 of the Securities Markets Law.
- 3.2 In addition to custodian services, a Custodian may also engage in the following services: (i) specific securities register activities, (ii) clearing activities arising out of or in connection with such registration activities, (iii) securities settlement activities and (iv) other regulated activities permitted by the Commission on each case as described in Articles 51.1.3-51.1.5 of the Securities Markets Law.
- 3.3 The Commission may choose to grant the license to carry out specific securities register activities and securities settlement activities together with [at the same time as] the license of custodian services.
- 3.4 A custodian shall perform the following specific functions as an integral part of custodian services set out in Section 3.1 of this Regulation:
  - 3.4.1. transfer securities, cash and settlements definitively for the client;
  - 3.4.2. sign with each beneficial owner of securities or its representative an individual Custody Services Agreement as described in Article 5 of this Regulation;
  - 3.4.3. record and keep separately the cash and securities of clients from those of the Custodian;
  - 3.4.4. record and keep separately the cash and securities of each Client from those of other Clients;
  - 3.4.5. for physical securities, ensure that the securities are whole describing each security's holder, classification and identification, hold each security separately in a safe and secure place;
  - 3.4.6. for dematerialised securities, ensure that each security is clearly and completely described in a digital system, including each security's holder, classification and identification, record each client's cash and securities separately from each other;
  - 3.4.7. maintain the securities database containing at least the following information:
    - 3.4.7.1. voting rights, date of the Annual General Meeting,
    - 3.4.7.2. any transfer restrictions,

- 3.4.7.3. information on taxation,
  - 3.4.7.4. other information as may be necessary for the custodian to carry out custodian services as described in Sections 3.32.1-3.32.8 of this Regulation.
- 3.5 Custodian shall perform corporate actions in a timely manner on behalf of the client as follows:
- 3.5.1. manage and participate in the corporate actions that apply to the safekept securities on behalf of the client in accordance with the Custody Services Agreement set out in Section 3.11 of this Regulation;
  - 3.5.2. obtain the relevant information about the corporate actions, communicate the information in written form to the client, carry out the instructions of the client on his behalf;
  - 3.5.3. in the absence of a written instruction from the beneficial owner or his representative on a corporate action, act in accordance with the provisions of the Company Law on shareholder rights and of the Custody Services Agreement;
  - 3.5.4. if provided for in the Custody Services Agreement, process any applicable taxation, including determining the tax obligations of the client, informing the client of his tax liability, paying the applicable taxes to or reclaiming overpaid taxes from relevant authorities;
  - 3.5.5. for all and any corporate actions, act in the interest of the client and ensure that the cash and securities of the client are kept separate from those of the Custodian. \
  - 3.5.6. The Custodian shall, upon request, provide to the issuer or to the CSD the list of shareholders (beneficial owners) and their respective shareholdings [in the issuer] as described in Article 64.1 of the Company Law.
  - 3.5.7. The Custodian shall offer, in writing, each client the possibility to attend the Annual General Meeting of Issuers in person or to make use of a proxy voting service. The Custodian shall keep the detailed records such as the date, agenda and information on Annual General Meetings as well as instructions of the client on voting on behalf of the client.
- 3.6 The Custodian may open and operate one or more cash accounts for the purpose of the client's settlement, which account(s) shall be subject to the following conditions:
- 3.6.1. The types, conditions and fees of the cash account(s) must be described in detail in the Custody Services Agreement;
  - 3.6.2. The Custodian must clearly separate in its digital system cash positions of each client from each other and from the Custodian's own positions;
  - 3.6.3. The Custodian must never use the money in a Client account for its own (Custodian's) needs;

- 3.6.4. The Custodian must ensure that all cash accounts of are reconciled and accurately managed and provide the client with statements that describe the most recent movements and positions in the cash account(s) at a frequency to be defined in the Custody Services Agreement.
- 3.7 The Custodian may receive collateral from a client, but must use such collateral only in the case of a default by the client or his representative to make the payment(s) and according to the applicable laws and regulations.
- 3.8 The Custodian must collect and provide to a client information with respect to the financial instruments held by the client, issuer(s) of such instruments and other information in accordance with the Custody Services Agreement.
- 3.9 Corporate actions are events in the life of a company that occur upon decisions by the Board of directors of a listed company and that directly impact its shares – whether common or preferred, shareholders or bondholders.
- 3.10 Corporate actions are not limited to the actions set out in Sections 3.13.1-3.13.16 of this Regulation.
- 3.11 Custodian must assist a client with the following [most common] corporate actions and may assist with other corporate actions described in the list in the appendix pursuant to the Custody Services Agreement:
- 3.11.1. Annual General Meeting of Shareholders, Extraordinary General Meeting of Shareholders;
  - 3.11.2. Acquisition;
  - 3.11.3. Capital Increase;
  - 3.11.4. Conversion of Equities and Debt Instruments;
  - 3.11.5. Coupon Payment of Debt Instruments;
  - 3.11.6. De-merger/Spin-Off/Merger;
  - 3.11.7. Dividend;
  - 3.11.8. Exchange;
  - 3.11.9. Liquidation;
  - 3.11.10. Proxy voting;
  - 3.11.11. Redemption of Debt Instruments;
  - 3.11.12. Split/Reverse Split;
  - 3.11.13. Tax Reclamation in case of Equities and Debt Instruments.
- 3.12 The Custodian shall perform each of the corporate actions set out in Sections 3.11.1-3.11.13 of this Regulation in the following manner:
- 3.12.1. For the corporate action indicated in Section 3.11.1 of the Regulation, the custodian must receive, in behalf of the clients, from the CSD an invitation to the

AGM. The custodian should send a copy of the invitation with the agenda to its clients and ask them if they want to vote in the AGM. If the clients want to vote, then they should appoint the custodian as their proxy and tell him how they want to vote at the AGM;

3.12.2. For the corporate action indicated in Section 3.11.2 of the Regulation, if the Custodian is holding client shares in the acquired company, then it must re-register those shares and adapt the client's shareholding to reflect the new situation after the acquisition;

3.12.3. For the corporate action indicated in Section 3.11.3 of the Regulation, if the shareholder receives subscription rights, then the Custodian must inform that shareholder of the exercise conditions and determine whether the shareholder wishes to exercise his rights. If the shareholder does, the Custodian should exercise the rights on behalf of the shareholder and accordingly manage the exercise process;

3.12.4. For the corporate action indicated in Section 3.11.4 of the Regulation, the custodian must inform the client of the applicable conditions of the conversion and ask the client if he wants to convert his securities. If the client decides to convert his securities, then the custodian should submit the convertible security and receive the resulting shares on behalf of the client. The custodian then holds the new shares in custody on behalf of the client and records accordingly;

3.12.5. For the corporate action indicated in Section 3.11.5 of the Regulation, the Custodian must verify and establish the entitlement of its clients to coupon payments before or on the appropriate record date. The Custodian must then ensure that the corresponding amounts are paid to it on behalf of its clients and then transfer the amount received to the client's account;

3.12.6. For the corporate action indicated in Section 3.11.6 of the Regulation, the Custodian must ensure that it obtains the complete information on the de-merger/spin-off/merger before it happens. Depending on the conditions of the de-merger/spin-off/merger, the Custodian may ask its clients if they want to participate in the de-merger/spin-off/merger or not. In any case, the Custodian must perform the required actions on behalf of its clients and credit the shares resulting from the de-merger/spin-off/merger to the clients' accounts;

3.12.7. For the corporate action indicated in Section 3.11.7 of the Regulation, the Custodian must verify and establish the entitlement of its clients to dividend payments before the appropriate record date. The Custodian must then ensure that the correct amounts are paid to it on behalf of its clients and then transfer the appropriate amount to each client's account, while keeping track of any money retained at source (such as a withholding tax, charges) (cf., "Tax Reclamation", below);

3.12.8. For the corporate action indicated in Section 3.11.8 of the Regulation, the Custodian must ensure that it receives the details of the exchange offer with sufficient anticipation so that its clients will have time to react. Once the Custodian has the information, it must provide it to its clients and ask them to decide if they want to take advantage of the exchange offer or not. If yes, then the custodian

executes the exchange and credits the resulting securities or cash to the client's account(s);

3.12.9. For the corporate action indicated in Section 3.11.9 of the Regulation, the Custodian must ensure that it receives complete information about the liquidation on time. It then informs its clients and attempts to recover the value of their shares from the liquidator/liquidation commission of the company. Any money that the Custodian receives from the liquidator/liquidation commission must be paid to the clients' accounts;

3.12.10. For the corporate action indicated in Section 3.11.10 of the Regulation, if the client appoints the Custodian as his proxy, then the Custodian must attend the shareholder meeting and vote on behalf of the shareholder. The custodian must follow the instructions provided by the client;

3.12.11. For the corporate action indicated in Section 3.11.11 of the Regulation, the Custodian must keep track of the maturity dates of the debt instruments held by the clients. When a debt instrument is redeemed, the Custodian must submit it to the issuer and receive payment for the par value of the instrument. The money received must be paid to the account(s) of the client;

3.12.12. For the corporate action indicated in Section 3.11.12 of the Regulation, the Custodian must ensure that it has complete information on the split/reverse split sufficiently in advance to adjust the equity's pricing and inform the client. Once the split/reverse split has been performed, the Custodian must apply the new conditions to the equities that it is holding and inform the client of the new value of his position;

3.12.13. For the corporate action indicated in Section 3.11.13 of the Regulation, the Custodian must first determine whether a double taxation treaty is applicable to the client's situation. If the client is entitled to a reimbursement of an amount overpaid, then the Custodian must calculate the exact amount. The Custodian must then find out the procedure that must be followed to obtain the reimbursement. Once the procedure is known, the Custodian must apply for the reimbursement on behalf of the client. When the reimbursement is received, the Custodian must credit the money to the client.

3.13 The Custodian must never use the securities or cash in a Client's account(s) without the written consent of the Client or his representative.

3.14 Specific securities registration shall comprise activities as described in Article 42 of the Securities Markets Law.

3.15 A Custodian who may carry out specific securities registration activities together with [at the same time as] custodian services shall meet the following requirements:

3.15.1. must be a member of the CSD as described in Article 42.4 of the Securities Markets Law and open and maintain an account with the CSD;

3.15.2. must maintain up-to-date information on the Beneficial Owner or his representative and, if applicable, the Nominee of any collective position, as well as any other additional information required by the Commission;

- 3.15.3. must maintain a database of the information described in Section 3.36 of this Regulation.
- 3.16 Both centralized and specific securities registers must reconcile. The Custodian must ensure the accuracy of the specific registers that it operates and reconciles the total in each register with the corresponding centralised position in the CSD.
- 3.17 A Custodian and/or the CSD that performs registration of securities ownership shall maintain in its entirety the registration of information pertaining to transfer of ownership for the period prescribed by regulations and shall report the corresponding information to the Commission and to the BoM.
- 3.18 A Custodian and/or the CSD that performs registration of securities ownership shall be responsible for the integrity, accuracy and completeness of the registration information, which it records in the securities register. The person who has entered wrong information shall be held liable for the damage caused.
- 3.19 A Custodian shall maintain up-to-date registration of any changes in the securities and/or in the ownership of the beneficial owner. Changes in the specific securities register shall be registered promptly in conjunction with the registration of changes to the centralised securities register as described in Article 42.4 of the Securities Markets Law.
- 3.20 A Custodian who may carry out securities settlement activities together with [at the same time as] custodian services per Article 51.1.4 of the Securities Markets Law.
- 3.21 Securities trade settlement shall comprise activities as described in Article 44.1 of the Securities Markets Law.
- 3.22 Securities trade settlements shall be made within the time period set out in Article 44.2 of the Securities Markets Law. Settlement shall be performed by the Custodian operating both a cash account and a securities account for the trades of its own and for the trades of its Clients.
- 3.23 The Custodian must ensure that at all times its Client's cash and securities are kept separate from those of the Custodian as described in Section 3.8 of this Regulation.
- 3.24 Trade settlement includes compiling and maintaining the proper financial records in accordance with the statement of payments and the executed transactions, entering that information, storing it in a database and delivering that information to the Beneficial Owner or his representative (including nominee) in the form of an account statement and/or report.
- 3.25 Trade settlement shall be settled exclusively on a delivery against payment basis.
- 3.26 Settlement is definitive once the seller has placed the money and the buyer has placed the securities in their corresponding accounts with the Custodian. Ownership rights to the settled securities are transferred definitively to the beneficial owner or his representative (including Nominee) only when the settlement is definitive.

- 3.27 The Commission, the BoM, the MSE, the CSD may issue detailed regulations, procedures and methodologies within their [respective] powers on securities trade settlement, either on its own or jointly with others.
- 3.28 Centralised securities registration shall be carried out by a legal person licensed to conduct securities central depository activities per Article 45.2 of the Securities Markets Law.
- 3.29 The person [licensed] to conduct securities central depository activities shall perform the following activities in addition to those described in the Securities Markets Law and in the Company Law:
- 3.29.1. To maintain the centralised securities register of all securities offered to the public;
  - 3.29.2. For each issue of shares, to track all changes [movements] of shares between CSD accounts and to reconcile daily with the securities specific register for each nominee;
  - 3.29.3. To keep a record of total amount of shares issued and outstanding, the most recent price of the shares published by the MSE, a description of the issuer of the shares and any other relevant information.
- 3.30. The securities register for each company shall be a unified system that is held separately from the register of other companies. The register shall have only one entry for each shareholder and represent the aggregate value of shares held by that shareholder. The CSD shall grant an International Securities Identification Number (ISIN) for each security based on the rules defined in the ISIN standard.
- 3.31. The CSD shall maintain complete information on all nominee positions (custodians) and, shall demand from the nominee the name of a beneficial owners upon a request by a securities, or where so required by the Company Law.
- 3.32. The centralized securities register shall contain the following information:
- 3.32.1. type of financial instrument (based on ISO 10962),
  - 3.32.2. name of the issuer,
  - 3.32.3. ISIN and other identification codes,
  - 3.32.4. nominal value, currency of the nominal value,
  - 3.32.5. place of listing,
  - 3.32.6. for the bonds, nominal value issued, currency of the nominal value, date of issue, place of listing, date of maturity, coupon rate, coupon payment date,
  - 3.32.7. for the shares, the description will also include date of AGM, transfer restrictions, taxes, special conditions,
  - 3.32.8. other information as required by the CSD.

#### **Four. General Obligations of a Custodian**

- 4.1. A Custodian shall comply with the following general obligations in its operations:
- 4.1.1. sign with each client an individual Custody Services Agreement based on the relevant documentation and materials that contains sufficient information about the client;
  - 4.1.2. when concluding a Custody Services Agreement, present to the client, if requested by the client, the Custodian's internal regulations, rules, financial reports, other documents and papers as prescribed by the relevant laws and regulations;
  - 4.1.3. ensure that all cash in the client's account(s) is clearly identified and segregated from the assets of the Custodian, safely kept and recorded in accordance with the Custody Services Agreement;
  - 4.1.4. inform the client of any transactions or transfers conducted in the client's account(s) by the business day following the date of the transaction in a form specified in the Custody Services Agreement;
  - 4.1.5. deliver to the client for its/his/her account(s) on a monthly basis statements of transactions conducted and holdings of securities and cash by digital communication or by another medium as requested by the client;
  - 4.1.6. retain the reports and data related to the client's active as well as closed account(s) and the transactions in it for at least 10 years and thereafter them over to a relevant entity for safekeeping;
  - 4.1.7. send the client's reports and account statements to the client by digital communication or by a hard copy as specified in the agreement;
  - 4.1.8. ensure the confidentiality and integrity of the client's account information contained in the internal recordkeeping system of the Custodian;
  - 4.1.9. inform the client within 3 (three) business days after receipt of any information received from the securities issuer, its agents and/or the CSD and designated for the client;
  - 4.1.10. separate or transfer assets in the client's account(s) only upon written instruction of the client or its/his/her representative or upon a decision of an authorized entity;
  - 4.1.11. provide other services as specified in the Custody Services Agreement.
- 4.2. A Custodian shall perform the following duties when keeping and recording a client's assets:
- 4.2.1. record the client's securities positions and ensure that the securities are available for a transaction at all times immediately upon the client's request;
  - 4.2.2. execute transfers related to the client's securities and cash positions in accordance with the applicable regulations;
  - 4.2.3. ensure that the rights related to securities are transferred to a client upon validation by the CSD;



- 4.2.4. other duties specified in the relevant legislation of Mongolia or in the Custody Services Agreement with the client.
- 4.3. A Custodian shall establish and operate a dedicated internal control unit which unit shall supervise the operations of the Custodian set out in Sections 4.1 and 4.2 of this Regulation.
- 4.4. In performing the services described in Sections 4.1 and 4.2 of this Regulation, the Custodian will perform the following specific functions as an integral part of its services:
- 4.4.1. create and operate the appropriate conditions and infrastructure for recording, safekeeping and maintaining positions and movements of assets in all client accounts;
  - 4.4.2. record and keep separately the assets of each client from the assets of the Custodian and the assets of other clients;
  - 4.4.3. receive and credit to a client's account(s) the securities or the proceeds from a buy or sell order, a corporate action or an interest payment;
  - 4.4.4. accurately and completely maintain the records and accounts of the securities and other assets as indicated in this Regulation and other relevant legislation;
  - 4.4.5. monitor and reconcile the positions held by each beneficial owner individually and/or jointly in shares of a listed company and comply with the holding thresholds and reporting requirements of Articles 22 and 23 of the Securities Markets Law and Article 57 the Company Law;
  - 4.4.6. disclose, within 3 days, to the Commission, upon the Commission's request, the detailed information on the shareholder(s) such as personal and financial data on the holdings;
  - 4.4.7. accommodate the conditions to supervise and review the information, reports and statements of a client's account(s) as well as in respect of Custodian's other activities during the Commission's supervision;
  - 4.4.8. fulfil the requirements of minimum amount of required capital, appropriate operational ratios and client protection from risk as described in Article 16 of this Regulation;
  - 4.4.9. submit to the Commission the quarterly financial statements approved by the executive director or the finance director prior to the 20th day of the following month;
  - 4.4.10. inform the Commission as soon as the Custodian becomes aware of financial, legal, market, operational or reputational risks that could negatively affect the financial position of the Custodian;
  - 4.4.11. In addition to the reports required in the Securities Markets Law and the Banking Law, submit the following monthly information to the Commission prior to the 25<sup>th</sup> day of a next month in the format defined in the annex of this Regulation:
    - 4.4.13.1. client information overview;
    - 4.4.13.2. size (amount) and value of the assets under Custody Services provided.

- 4.5. If a Custodian is a bank's controlled company or subsidiary, such Custodian shall inform and obtain consent of the Commission each time when making changes to its shareholders, the paid-in capital, the legal entity's name or appointing or dismissing its executive director

### **Five. Custody Services Agreement**

- 5.1. A Custodian shall provide custodian services with respect to the safekeeping and administration of securities and cash, as well as other services described in the legislation and this Regulation based on the Custody Services Agreement signed with the client.
- 5.2. It is prohibited for a Custodian to perform any Custodian services for a client without signing the Agreement indicated in Section 5.1 of this Regulation.
- 5.3. A Custodian is required to introduce the relevant legislation to a client before entering into any Custody Services Agreement with the client.
- 5.4. A Custodian may sign a Custody Services Agreement with the client without regard to where the client is located.
- 5.5. The following minimum terms and conditions must be included in the Custody Services Agreement, in addition to those set out in the Civil Code and other relevant legislation:
- 5.5.1. types and forms of custody services, rights and responsibilities of the client and the Custodian;
  - 5.5.2. the amount of the fees for the custody services and the related information;
  - 5.5.3. regulation on suspension of Custody Services and termination of the agreement;
  - 5.5.4. compensation;
  - 5.5.5. reporting obligations to the Commission and to the BoM;
  - 5.5.6. procedure on terminating the Agreement;
  - 5.5.7. types of information to report to the client and the frequency and format of reporting;
  - 5.5.8. procedure on returning the assets in the client's account or transferring them to another Custodian;
  - 5.5.9. procedure on ensuring the safety and security of the client's assets and reconciling securities and cash;
  - 5.5.10. procedure on conversion of a currency in the event of transfers by a foreign investor in a currency other than MNT;
  - 5.5.11. force majeure conditions;
  - 5.5.12. scope of applicable law and dispute resolution.
- 5.6. If the Custody Services Agreement is terminated at the request of a party other than the party indicated in Section 5.7 of this Regulation [i.e., at the request of the client], the net assets in the client's account that remain after covering any negative positions or debts [of the client] shall be transferred to the client's account at another Custodian within 20 (twenty) business days based on the client's written request.

- 5.7. If the Custody Services Agreement is terminated at the initiative of the Custodian, the Custodian shall transfer to the new Custodian the client's net assets that remain after covering any negative positions or debts [of the client] in accordance with Section 14 of this Regulation.
- 5.8. The Custodian may hold the securities of the client in the CSD in a collective account for which the Custodian is the nominee, or the Custodian may open an individual account in the CSD for a specific client, in which case only the Custodian will operate the account as nominee on behalf of the specific Client. All nominee accounts operated by a Custodian are subject to the following conditions:
- 5.8.1. the policies and procedures for maintaining and operating a nominee account must be explained to the client in the Custody Services Agreement, which the client must approve and sign;
- 5.8.2. if the client's assets are held in a collective account in the name of the Custodian as nominee, the Custodian must clearly segregate and identify all the client's holdings within its internal recordkeeping and systems;
- 5.8.3. in order to facilitate the segregation of the holdings of the Custodian from those of its clients, at least two collective accounts shall be opened and operated in the CSD – one account for the assets of the Custodian and another account for the assets of its clients;
- 5.8.4. the collective accounts registered in the name of the nominee shall be reconciled on a regular basis with the individual assets of the clients in the nominee's internal recordkeeping. The Custodian shall perform such reconciliation on a weekly basis and report any material discrepancies to the Commission within one calendar week of discovering such discrepancies;
- 5.8.5. the rules applying to a collective account shall comply with relevant laws and regulations of Mongolia.
- 5.9. Subject to the relevant laws and regulations, the client may open a fully disclosed account registered in the client's name in the CSD. The Custodian shall comply with the following conditions in operating such account on behalf of the client:
- 5.9.1. the fully disclosed account shall be opened at the CSD with the following name: "Name of Custodian on behalf of name of Client" (e.g., "Account of Bank X on behalf of Mr Y");
- 5.9.2. if the client has requested opening a fully disclosed account at the CSD the Custodian shall include the following information in the Custody Services Agreement:
- 5.9.2.1. the rights and responsibilities of the client with regard to the operation and maintenance of the disclosed account;
- 5.9.2.2. the degree to which the Custodian is involved with the operation and maintenance of the fully disclosed account;
- 5.9.2.3. the obligations of the CSD towards the client;
- 5.10. A Custodian shall have the right to determine the terms and conditions of the Custody Services Agreement. The Commission shall not regulate the Agreement in any manner other than as described in Section 5.5 of this Regulation.

**Six. Records of Assets in Client Account(s), Reconciliation of Assets**

- 6.1. A Custodian shall record the client's assets off-balance sheet in its [Custodian's] internal books and records and such recording shall comply with the following requirements:
  - 6.1.1. there shall be a separate account for each client within the internal recordkeeping and accounting of the Custodian. Transactions in each such account shall be processed and recorded according to the international professional standards applicable to custody accounting;
  - 6.1.2. when servicing Mongolian-registered securities held on behalf of a foreign investor, the Custodian shall open an account at the CSD in the name of the foreign investor or the corresponding foreign custodian with whom the Custodian has an agreement. The Custodian shall ensure that it acquires and maintains all the necessary information about the foreign investor and [the corresponding foreign] custodian as described in Section 7.7 of this Regulation;
  - 6.1.3. the Custodian must ensure the safekeeping of the client's cash and securities and reconcile those assets against the records of the CSD for Mongolian-registered securities or, for foreign-registered securities, against the records of the foreign custodian;
  - 6.1.4. in performing the reconciliation specified in Section 6.1.3 of this Regulation, the Custodian shall comply with the relevant laws as well as rules and regulations issued by the CSD.
- 6.2. A foreign custodian shall provide the Custodian with the necessary information per Section 7.7 of this Regulation.
- 6.3. A Custodian shall, together with the CSD, verify and reconcile the assets in the client's account(s) on a weekly basis and issue an exception report as a result of such reconciliation. The exception report shall identify any discrepancies either on a nominee account or a disclosed account and the proof of their [discrepancies'] final resolution.
- 6.4. The exception report shall be executed in 2 (two) copies and endorsed with the signatures and stamps of the parties involved.
- 6.5. When reconciling with a foreign custodian or with a foreign CSD, a Custodian shall use a secure automated system for international inter-bank information transmission as specified in the [relevant] agreement. During the reconciliation process, the securities balances in the client's account in the Custodian's internal system shall be determined as of the date of the reconciliation.
- 6.6. The documents and records used for reconciliation and the information received through the [secure automated] system shall be transferred to the CSD and retained for at least 10 years after the reconciliation date.
- 6.7. If a discrepancy over the balances in a client's account is found as a result of the reconciliation, the parties involved in the reconciliation shall take the necessary measures to correct the discrepancy.

- 6.8. If a discrepancy found during the aforementioned reconciliation could not be resolved and continues to be outstanding until the next exception report is issued, such discrepancy shall be immediately reported to the Commission, the BoM and the CSD.
- 6.9. The CSD shall support without any obstacles the Custodian in acquiring the information necessary for the reconciliation specified in this Regulation.

### **Seven. Types of Accounts**

- 7.1. A centralised securities register in the CSD shall comprise a collective position of all securities and a specific securities register with a Custodian shall comprise the assets of individual beneficial owners or their representatives.
- 7.2. A Custodian can have the following types of accounts:
  - 7.2.1. a fully disclosed account or direct holdings account – an account opened and operated in the name of a beneficial owner. The information on the [registered] holder of the account shall be the information of the beneficial owner;
  - 7.2.2. a nominee account or indirect holdings account – an account operated by a nominee on behalf of others. The nominee account information shall be the information of the nominee, not of the beneficial owner. The nominee shall hold securities, executing transactions on behalf of the beneficial owner and on the basis of instructions from the beneficial owner or his representative;
  - 7.2.3. a mixed or modified holdings account – a type of nominee account. Such account shall reveal the name of the beneficial owner, but the nominee shall be allowed to perform transactions on behalf of the beneficial owner without instructions from the beneficial owner;
  - 7.2.4. a trustee account - a trustee account shall be operated by a trustee on behalf of a beneficial owner at the trustee's discretion without instructions from the beneficial owners, but in interest of the beneficial owners.
- 7.3. A fully disclosed account shall contain the following information:
  - 7.3.1. the account shall be opened in the name of a beneficial owner and shall contain the following information about the beneficial owner – fully name, registration [passport] number, address, telephone number, e-mail address, relevant tax authority, marital status, number of children, source of funds, copy of passport; if the beneficial owner is a legal person, number of state registration and certificate, identity of the authorised signatory;
  - 7.3.2. through a power of attorney or a permanent instruction, the beneficial owner may appoint a representative to operate the fully disclosed account on his behalf, but the securities in the account shall remain the property of the beneficial owner only. The representative shall be qualified and authorised to operate accounts on behalf of others.
- 7.4. A nominee account shall have the following characteristics:

- 7.4.1. the nominee operating the account shall be a legal entity that has been authorised by the Commission to act as a Custodian;
- 7.4.2. the beneficial owner shall appoint the nominee through a Custody Services Agreement;
- 7.4.3. the nominee /the Custodian/ shall, in its internal bookkeeping, open an account for each beneficial owner containing the information specified in Section 7.3.1 of this Regulation;
- 7.4.4. the nominee /the Custodian/ shall, in its internal bookkeeping, reconcile assets of each beneficial owner in the collective position in any nominee account.
- 7.5. A mixed account shall be subject to the same conditions as a nominee account, but a mixed account shall reveal the name of the beneficial owner. A mixed account, therefore, shall contain complete information on the beneficial owner similar to a fully disclosed account, but shall be operated by a Custodian only.
- 7.6. A trustee account shall be opened and operated based on a formal trustee agreement between the trustee and the beneficial owner. The agreement shall describe the mutual rights and responsibilities of the trustee and the beneficial owner. The trustee shall, in its internal system, open an account for each beneficial owner containing the information specified in Section 7.3 of this Regulation and reconcile assets of each beneficial owner in the collective trustee account. The nominee /the Custodian/ shall, in its internal bookkeeping, reconcile assets of each beneficial owner in the collective trustee account.
- 7.7. For all types of accounts set out in Section 7.2 of this Regulation, a Custodian shall perform the appropriate level of due diligence on clients as a means of preventing money laundering, terrorist financing or other economic crimes and as a way of ensuring the creditworthiness of their clients:
  - 7.7.1. in performing due diligence, a Custodian shall follow the Law of Mongolia on Combating Money Laundering and Terrorist Financing, including the procedure described in Article 5.3 therein;
  - 7.7.2. for existing clients, a “grandfathering” approach shall be acceptable for opening accounts in the name of the beneficial owner;
  - 7.7.3. due diligence shall be performed according to a risk-based approach as recommended by the Financial Action Task Force, involving three levels of due diligence in accordance with the perceived level of risk:
    - 7.7.3.1. simplified [minimal level of] due diligence shall be used for clients perceived as low risk;
    - 7.7.3.2. standard due diligence shall be used for typical clients involving, for individuals, a signed application form, a copy of the beneficial owner's passport, proof of residence and a source of funds declaration; for legal persons, a list of authorised signatories of the beneficial owner, copies of passports of each signatory, source of funds declarations and any other documentation required by the BoM;
    - 7.7.3.3. enhanced due diligence shall be used for clients perceived as high risk, such as politically influential persons, or clients located in foreign countries that

are deficient in preventing money laundering and terrorist financing as determined by an international organisation with the function of preventing money laundering and terrorist financing, or remote clients, involving the following:

7.7.3.3.1. apostille-notarised photocopies of the documents specified in Section 7.7.3.2 of this Regulation, plus additional information, proof of profession, criminal record from the police in the country of residence;

7.7.3.3.2. if the client is a foreign financial institution, the due diligence on the beneficial owner of the foreign financial institution shall be conducted as follows:

7.7.3.3.2.1 determine if [potential] money laundering and terrorist financing activities of the foreign financial institution is subject to “equivalent supervision” by a relevant authority of that country;

7.7.3.3.2.2 the Custodian may delegate the function of due diligence on the beneficial owner to the foreign financial institution, but the Custodian shall remain responsible to the BoM and the Commission for ensuring that the due diligence is properly conducted;

7.8. The Custodian shall evidence the obligations and responsibilities of the foreign financial institution in relation to the due diligence by describing such obligations and responsibilities in the Custody Services Agreement when opening an account for the foreign financial institution /nominee/.

7.9. A Custodian shall have the appropriate organisation, staff and procedures for the prevention of money laundering and terrorist financing as required by the BoM in accordance with the Law [of Mongolia] on Combating Money Laundering and Terrorist Financing.

## **Eight. Infrastructure for Custody Services**

8.1. A Custodian shall have the obligation to provide a secure and professional custody operations and shall maintain an infrastructure comprising the following components:

8.2. Secure physical premises which shall meet the following requirements:

8.2.1. the premises shall be in a location where they shall not be exposed to flooding, fire or damage by extreme weather conditions; the building, windows, doors and the associated locks shall be sufficiently strong;

8.2.2. the premises shall have sufficient lighting according to international standards and an emergency generator to ensure that the Custody Operations Unit can continue operating in the case of a power outage;

8.2.3. the premises shall be equipped with the following facilities: the alarm system with sensors, the appropriate temperature controls, smoke alarms, sprinklers and sufficient fire extinguishers to manage effectively emergency situations, such as all types of fire, extreme heat or cold, flooding etc.;

- 8.2.4. the workspace of each employee shall be at least 6 (six) square meters and include a desk, an office chair, adequate lighting, a telephone, a PC and other components;
- 8.3. The IT environment which shall be secure and properly equipped, including the following components:
  - 8.3.1. a secure computer room for any central computer and telecommunications equipment,
  - 8.3.2. a properly equipped computer room with a raised floor, temperature control, adequate ventilation, a locking fire-resistant door and no windows;
  - 8.3.3. secure telephone and data lines provided by a reliable and stable telecommunications company, a "soft" and a "hard" firewall;
  - 8.3.4. secure and reliable connections to the telecommunication applications of the CSD and MSE; conformity of protection and security of the data transmission to the proper international standards;
  - 8.3.5. a voltage stabiliser to protect against fluctuations in the flow of electricity, an uninterrupted power supply (UPS) that shall allow independent operation of the central computer and all telecommunications equipment for at least 4 hours;
  - 8.3.6. the central system, including the specialised software, archived documents and locally stored E-mails, shall be backed up in real time to a computer located in separate facilities outside the Custody Operations Unit; back-up storage media shall be stored in secure facilities off-site, i.e., in a fire-resistant data safe in a secure building that is separate from the operational site;
- 8.4. The hardware environment which shall be secure and reliable, including the following components:
  - 8.5.1. a dedicated central computer with sufficient speed, memory, security ("hard" firewall)
  - 8.5.2. a server for a minimum of 50 user PCs, Internet access, storage space for documents and E-mail;
  - 8.5.3. each employee shall have his/her own PC with sufficient speed, memory and storage space to run MS Office applications and the specialised custody software; for security reasons, USB ports, CD/DVD drives and any other output facilities shall be locked and only accessible to the IT administrator;
- 8.5. the software required for the Custodian or the Custody Operations Unit shall comprise the following:
  - 8.5.1. a basic system software for the central computer /which shall be Windows Server or another standard operating system/;
  - 8.5.2. an appropriate security software, which shall include a user administration software, a firewall, a virus checker and other software that enhances the security of the central computer;



- 8.5.3. a telecommunication software which shall allow secure access to telecommunications applications, including a LAN within the Custody Operations Unit, SWIFT, the transaction processing and reporting systems of MSE, the CSD and the BoM, the Internet and secure E-mail connectivity;
  - 8.5.4. an office software which shall be installed on the central computer for managing E-mail, document storage, a calendar and any other software required for normal office applications;
  - 8.5.5. a custody management software which shall be installed on the central computer; this software may be a package or proprietary; it shall provide the functionality required to run custody operations (e.g., a securities database, a client database, account management software, applications for generating and managing instructions etc.);
- 8.6. Use protection technology in data transfer in order to preserve the integrity of the information security. A business continuity plan which shall have the following characteristics:
- 8.6.1. the business continuity plan shall cover all aspects of the normal and stable operation of custody services;
  - 8.6.2. the business continuity plan shall cover all operational elements of the Custody Operations Unit, including computers, other hardware, data communications, telephone, fax, printing, staff etc.;
  - 8.6.3. the business continuity plan shall be updated regularly;
  - 8.6.4. the business continuity plan shall be included in the annual audit of the Custody Operations Unit;
  - 8.6.5. the business continuity plan shall be tested [by the Custodian] at least once a year; the test may not be announced to the staff beforehand and the results of the test shall be recorded formally in a test report which shall be submitted to the Commission;
- 8.7. all processes in the Custody Operations Unit (particularly all aspects of the IT operation) shall be documented in accurate and comprehensive rules and procedures which shall be subject to the following requirements:
- 8.7.1. updated regularly;
  - 8.7.2. accessible to all employees of the Custody Operations Unit;
  - 8.7.3. included in the annual audit of the Custody Operations Unit.

### **Nine. Requirements for Management and Organization of a Custodian**

- 9.1. The highest authority in a Custodian shall be the shareholders meeting.
- 9.2. The Board of Directors shall be the governing body [of a Custodian] in between the shareholders meetings.

- 9.3. If the Custodian is a bank or a CSD, the Board of Directors shall be subject to requirements as described in the Banking Law [of Mongolia] and the Company Law [of Mongolia].
- 9.4. If the Custodian is a bank's controlled company or subsidiary, then it [Custodian] must have at least 3 board members, of which at least one must be an independent member per the Banking Law and the Company Law.
- 9.5. If the Custodian is a Custody Operations Unit, then its [the Unit's] management shall be the management of the bank and the bank's management committee shall meet at least once in a quarter in order to review the report on the custodian operations.
- 9.6. The functions of the Board of Directors shall be governed by the Company Law and the Banking Law as well as by the internal regulation on the Board of Directors.
- 9.7. The Custodian shall employ not less than 6 (six) full-time people as stated in Section 2.2.4 of this Regulation.
- 9.8. Although each Custodian may organise its operations differently, they shall seek to follow with the following indicative HRs and management structure:
  - 9.8.1. Custodian operations shall overall be managed by a chief executive officer or a manager who shall have a university degree in finances, as well as with work experience in the same field of at least 5 years and who shall have the following specific functions:
    - 9.8.1.1. to ensure the profitability of the custody services;
    - 9.8.1.2. to define, organise and ensure the successful execution of the policies, procedures and the work carried out in the Custody Operations Unit;
    - 9.8.1.3. to manage and lead the staff, to act as Secretary of the Management Committee.
  - 9.8.2. The IT Manager shall have the following specific functions:
    - 9.8.2.1. to ensure normal functioning of hardware, software, telecommunications, computer-related processes and procedures in custody services;
    - 9.8.2.2. to manage the IT risk and security;
    - 9.8.2.3. to manage the budget and costs of IT;
    - 9.8.2.4. to ensure that the IT applications are separate from other information in the parent bank.
  - 9.8.3. The Custody Specialist shall have a university degree in finances and work experience of at least 3 years and shall have the following specific functions:
    - 9.8.3.1. to perform all the tasks required by a client or to deliver custody services;
    - 9.8.3.2. to execute corporate actions, settle trades, produce reports, submit to relevant persons;
    - 9.8.3.3. to provide tax services, ensure ethical compliance;
    - 9.8.3.4. other functions as specified in custody service related agreement(s).
  - 9.8.4. The Customer Service Specialist shall have the following specific functions:

- 9.8.4.1. to manage relationships with customers and provide effective customer service;
  - 9.8.4.2. to answer customer queries promptly and accurately, to supply relevant information [to clients];
  - 9.8.4.3. to seek comments and suggestions from customers, to effectively resolve any issues raised by a customer, to ensure that customers receive statements, reports and other information.
- 9.8.5. The Custody Support Staff shall have the following specific functions:
- 9.8.5.1. to create forms, request documentation from customers, copy or archive [file] documents;
  - 9.8.5.2. to ensure the completeness of custody services agreements and other documentation files;
  - 9.8.5.3. to perform any other support functions required by the Custody Operations Unit or by the person specified in Sections 9.8.1-9.8.4 of this Regulation.
- 9.9. A Custodian shall maintain adequate insurance to cover the risks [to which it is exposed].

#### **Ten. Requirements for Risk Management**

- 10.1. A Custodian shall deposit the reserve in a special account in the BoM based on the value of securities that it holds under custody in order to cover operational risks to the financial system resulting from custodian services expressed as a percentage defined by the BoM.
- 10.2. A Custodian shall carry out reserve-adjusting transactions at the end of each year.
- 10.3. A Custodian shall create a risk management unit which unit shall have the following characteristics: report to the management of the Custodian on the risk management;
- 10.3.1. be managed by the relevant managers of the Custodian;
  - 10.3.2. issue and follow risk management policies for all types of risk to which the Custodian is exposed (such as market risk, credit risk, counterparty risk, operational risk, liquidity risk);
  - 10.3.3. conform to best international market practice for risk management using both quantitative and qualitative methods, such as value at risk and stress testing;
  - 10.3.4. follow the risk management cycle that comprises the following steps: Risk Identification, Risk Assessment, Risk Control and Mitigation, Risk Reporting, Risk Treatment, Risk Monitoring;
  - 10.3.5. operate and maintain a historical database of incidents and losses;
  - 10.3.6. have adequate qualified resources to effectively operate the risk management function;
  - 10.3.7. regularly produce reports on risk data that shall be submitted to the Commission on a quarterly basis.

### **Eleven. Restrictions and Prohibitions on Custody Services**

- 11.1. The following is prohibited for a Custodian in addition to any other prohibitions as described in the legislation:
- 11.1.1. making use of the securities or cash in a client's account(s) without the consent of the client or his representative;
  - 11.1.2. keeping the securities or cash of a client in the same account with the assets of the Custodian or in the same account with the assets of other clients;
  - 11.1.3. revealing to any third party the confidential and internal information, data, reports or documents obtained during the performance of custody services for the purpose of ensuring information security or for any other purpose, except when required by an authorized entity;
  - 11.1.4. disclosing or informing others of the name of a client or of other information in respect of his account;
  - 11.1.5. disclosing or informing others of the custody services or of the account of a client;
  - 11.1.6. engaging broker or dealer operations;
  - 11.1.7. other actions prohibited by the applicable laws or regulations or by the authorized entities.

### **Twelve. [Annual] Report on Custody Services**

- 12.1. A Custodian shall submit, upon approval by the Custodian's internal auditor and the Board of Directors, an annual report on the custodian unit to the Commission within the first quarter of the next year which report shall contain the following information:
- 12.1.1. all and any operations [of the Custodian] for reported year;
  - 12.1.2. annual financial statements, including the custody services [provided by the Custodian Operations Unit] and notes to the financial statements;
  - 12.1.3. information regarding all types of custody services;
  - 12.1.4. total number and the breakdown of all clients [by service];
  - 12.1.5. financial statements of the entire custodian entity or its Custody Operations Unit;
  - 12.1.6. financial status and reputation of the Custodian;
  - 12.1.7. debts and liabilities and obligations to others of the entire custodian entity or its Custody Operations Unit;
  - 12.1.8. independent auditor's report regarding the internal audit structure of the Custodian and its effectiveness;
  - 12.1.9. information regarding conflict-of-interest transactions or large transactions<sup>4</sup>;
  - 12.1.10. in case of the a custodian bank, corporate governance principles and their implementation;
  - 12.1.11. other information with respect to entire custodian entity or its Custody Operations Unit.

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<sup>4</sup> Translator's note: "conflict-of-interest" transactions and "large" transactions are defined in the Company Law (Article 89 and Article 87, respectively).

### **Thirteen. Suspending or Terminating a License**

- 13.1. The Commission may suspend a license of a Custodian for the following reasons:
  - 13.1.1. failing 3 (three) or more times to inform or report and deliver information as set forth in this Regulation;
  - 13.1.2. failure to submit due financial statements to the Commission or to other related organisations for two consecutive quarters;
  - 13.1.3. failure to pay the regulatory service fee established by the Commission for three months since the due date;
  - 13.1.4. concealing mistakes related to maintenance and reconciliation of a client's securities and/or cash records;
  - 13.1.5. proven repeated falsification of advertisements or false information that led to public confusion;
  - 13.1.6. any material circumstances that prevent the Custodian from providing the custody services in accordance and compliance with this Regulation;
  - 13.1.7. any serious breach of the Custody Services Agreement [by the Custodian];
  - 13.1.8. other reasons stipulated in the applicable laws and regulations.
- 13.2. If a license is suspended [by the Commission], the custodian that held the license may apply to the Commission to reinstate the license, if it deems that it has eliminated the reasons that led to the suspension of the license and it is in compliance with this Regulation.
- 13.3. The Commission may terminate a license of a Custodian for the following reasons:
  - 13.3.1. the Custodian filed such a request itself;
  - 13.3.2. the BoM terminated the banking license of the Custodian;
  - 13.3.3. the Custodian failed to pay the regulatory service fee established by the Commission for a period of over a year;
  - 13.3.4. the Custodian did not act to meet the minimum capital and/or reserve requirements for operational risks or the appropriate capital and/or reserve ratios as defined by the Commission and the BoM for 2 (two) consecutive quarters;
  - 13.3.5. the Custodian failed to perform custody services for more than 1 (one) year since the issuance of its license by the Commission;
  - 13.3.6. the Custodian failed to submit the required financial statements to the Commission for 2 (two) consecutive quarters;
  - 13.3.7. it became known that fraudulent documents were used [by the applicant] in obtaining the license from the Commission;
  - 13.3.8. the Custodian failed to fulfil the obligations assigned by the Commission during the suspension period of the License, or continued to run its activities during the suspension, or did not completely eliminate the violations that caused the suspension;

- 13.3.9. the Custodian was declared bankrupt by a court;
- 13.3.10. other reasons stipulated in the applicable laws and regulations.
- 13.4. If a license is terminated, it shall be seized and sealed with an “INVALID” stamp and placed in the file of the relevant entity and the file shall be transferred to the archive in accordance with the applicable regulation.
- 13.5. If a license is terminated, the Commission, the CSD and the Custodian shall establish a working group and transfer the remaining documents, records, reports, statements, data, and information associated with Clients or with custody services to another Custodian in accordance with the applicable procedure. The Commission shall transfer to its archives the documents, records, reports, statements, data, and information that may not be transferred to the new Custodian.
- 13.6. If a license is suspended, or reinstated, or terminated, the Commission shall give a corresponding notice to the Custodian within 3 (three) working days [after the decision is made] as well as to the public.
- 13.7. Individuals who worked at the entity with the terminated license or any legal entity shall be prohibited from using the name of the entity with the terminated license.

#### **Fourteen. Transferring Clients' Assets to a New Custodian**

- 14.1. If a Custodian other than a Custodian bank becomes bankrupt, or is liquidated, or if it issued a request to stop functioning as a Custodian, then the assets of the client(s) shall be transferred to another Custodian after approval by the Commission and upon presentation of the following documents:
  - 14.1.1. list of the assets being transferred;
  - 14.1.2. list of documents being transferred;
  - 14.1.3. list of the securities recorded in the clients' accounts by each client;
  - 14.1.4. a Custody Services Agreement for each client;
  - 14.1.5. statement of delivery and acceptance of the assets and documents;
  - 14.1.6. other applicable documents.
- 14.2. If a Custodian bank becomes bankrupt, or is liquidated, or if it issued a request to stop functioning as a Custodian bank, then the securities of the client(s) shall be transferred to another Custodian after approval by the Commission and upon presentation of the documents as described in Sections 14.1.1-14.1.6 of this Regulation.
- 14.3. The list of assets being transferred as mentioned in Section 14.1.1 of this Regulation, shall include all assets belonging to clients that were registered and kept by the Custodian in nominee accounts.
- 14.4. The list of documents mentioned in Section 14.1.2 of this Regulation shall include:
  - 14.3.1. statement of the account opened in a client's name in the internal bookkeeping of the Custodian and, if applicable, a statement of the account opened in the client's name at the CSD as of the date of transferring the assets;

- 14.3.2. statements of reconciliation of the client's assets with the CSD and with the client produced on the date of transfer by the Custodian and the documents used for such reconciliation.
- 14.5. When transferring assets to a new custodian, a statement on transferring the assets and documents shall be issued and the following information shall be included in that statement:
  - 14.4.1. date of the statement on transferring the assets;
  - 14.4.2. date of concluding the Custody Services Agreement between the client and the new Custodian that will serve the client;
  - 14.4.3. information about the client whose assets are being transferred;
  - 14.4.4. cash and securities in the client's account with the new Custodian as of the date of the statement on transferring the assets;
  - 14.4.5. list of documents to be transferred to the new Custodian;
  - 14.4.6. relevant information and signatures of all the parties involved;
  - 14.4.7. other necessary information.
- 14.6. A statement on transferring the Client's assets shall be verified by stamps of the former Custodian and of the new Custodian and by the signatures of the respective executive directors and chief accountants and shall be executed in 4 (four) copies, delivering 1 (one) copy to the client or its representative, 1 (one) copy to the former custodian, 1 (one) copy to the new Custodian and 1 (one) copy to the CSD.

### **Fifteen. Monitoring, Control and Responsibilities**

- 15.1. The Commission shall conduct remote and on-site scheduled and unscheduled monitoring and control of the activities of a Custodian and hold that entity liable, if necessary, according to the provisions of the applicable laws and regulations. The Commission shall deliver findings and results of its monitoring and control of the activities, if it deems it necessary. In the event the Custodian is a Custodian bank, the BoM and the Commission shall jointly conduct on-site investigation.
- 15.2. The Commission and the BoM shall conduct remote and on-site investigation of the following and any other activities of the Custodian:
  - 15.2.1. compliance with relevant laws and regulations;
  - 15.2.2. internal rules, regulations, instructions, contracts and their implementation;
  - 15.2.3. obligations under the Custody Services Agreement concluded with a client and their fulfillment;
  - 15.2.4. financial activities of the Custodian;
  - 15.2.5. minimum amount of the capital requirement and adequacy ratios;
  - 15.2.6. meeting the reliability of the client's assets;
  - 15.2.7. resolution of any conflicts of interest situations;
  - 15.2.8. arrangement of the internal operations of the Custodian;

- 15.2.9. internal processes of using, storing and protecting information;
  - 15.2.10. reporting of required data, information and statements to the Commission or the BoM according to the applicable laws and regulations;
  - 15.2.11. delivery of information to clients and the general public;
  - 15.2.12. meeting the safety, reliability and equipment of the information technology as required by the Commission and the BoM;
  - 15.2.13. Other documents that the Commission deems necessary.
- 15.3. If any violation of relevant laws and regulations is found during the process of monitoring and control as set forth in Section 15.1 of this Regulation, it shall serve as a reason for suspending or terminating the license of a Custodian.
  - 15.4. A Custodian shall compensate the loss resulting from its non-fulfillment of obligations as specified in the **Mongolian** laws and regulations.
  - 15.5. A Custodian shall not be held responsible and liable for the Client's own investment decisions.
  - 15.6. The Commission shall monitor the enforcement of this Regulation and hold responsible any entity that violates pursuant to applicable legislation.

#### **Sixteen. Reporting Requirements to FRC and the BoM**

- 16.1. A Custodian shall report within two weeks following the end of each calendar month to the Commission the transactions in securities that they have processed for their own account or on behalf of their clients.
- 16.2. A Custodian shall submit reports to the Commission in electronic form which reports shall meet the following requirements:
  - 16.2.1. ensure the security and confidentiality of the data reported;
  - 16.2.2. incorporate mechanisms and methods for identifying and correcting errors in a transaction report;
  - 16.2.3. incorporate mechanisms and methods for authenticating the source of the transaction report;
  - 16.2.4. be capable of reporting the information in the format required by the Commission and the BoM.
- 16.3. The transaction reports shall contain the following information for each security:
  - 16.3.1. Category attributed by a regulation issued by Commission to identify the transaction executed by the Custodian;
  - 16.3.2. the date and time of the transaction;
  - 16.3.3. the type of transaction (i.e., buy or sell) from the perspective of the reporting Custodian **bank**;
  - 16.3.4. whether the transaction was executed on the Custodian's own account or for the account and on behalf of a client;



- 16.3.5. description of the financial instrument processed in the transaction;
- 16.3.6. classification (according to ISO 10962) and identification (ISIN) of the financial instrument processed in the transaction;
- 16.3.7. maturity date of a bond;
- 16.3.8. the market price per security in the transaction, excluding commission and accrued interest; in the case of bonds, the price may be expressed either in terms of currency or as a percentage;
- 16.3.9. currency in which the price is expressed or, for a bond, price expressed as a percentage, the exact percentage applied;
- 16.3.10. number of shares or, for bonds, the nominal value of the transaction;
- 16.3.11. identification of the counterparties in the transaction;
- 16.3.12. identification of the trading place where the transaction was executed [e.g., MSE, over the counter];
- 16.3.13. indication as to whether the transaction was cancelled.

#### **Seventeen. Liability**

- 17.1. A person who is in breach of this Regulation shall be subject to liability under the Securities Markets Law, the Banking Law the Law of Mongolia on Combatting Money Laundering and Terrorism Financing and other applicable legislation.
- 17.2. No liability shall be imposed on the implementation of the Custody Services Agreement under this Regulation.

## **Annex I of the Regulation on Custodian Licensing and Custodian Services**

### **A list of other Corporate Actions which can be provided to a Client through a Custody Services Agreement**

- **Absorption.** Absorption of a new issue of stock into the parent security where the original shares did not fully rank pari passu with the parent shares. After the event, the assimilated shares rank pari passu with the parent, meaning that they carry exactly the same entitlements and rights.
- **Acquisition.** In general, companies will aim to grow. Growth can be achieved *organically* (the company simply grows their existing company) or *inorganically* (by acquiring other already existing businesses and integrate them with their own).
- **Bankruptcy.** Bankruptcy is the business decline of a company caused by its liabilities exceeding the fair market value of its assets.
- **Bonus Issue.** Existing shareholders are awarded additional securities free of payment.
- **Bonus Rights.** Distribution of rights which provide existing shareholders the privilege to subscribe to additional shares at a discounted rate.
- **Cash Dividend.** A distribution of cash to the shareholders of a company based on the performance of the company made out of the earnings at the end of the year.
- **Class Action.** A civil lawsuit is being made against the company (usually by a large group of shareholders or by a representative person or organisation) that may result in a payment to the shareholders.
- **Delisting.** The process of removing the security from a stock exchange.
- **De-merger.** One company de-merges itself into 2 or more companies. The shares of the old company are booked out and the shares of the new companies will be booked in according to a set ratio.
- **General Announcement.** An event used by the company to notify its shareholders of any events that take place. This event type is used to communicate several types of information to the shareholders.
- **Initial Public Offering.** The first time that a company gets listed on a stock exchange is regarded.
- **Liquidation.** Liquidation proceedings consist of a distribution of cash and/or assets.
- **Mandatory Exchange/Mandatory Conversion.** Conversion of securities (generally convertible bonds or preferred shares) into a set number of other forms of securities.
- **Merger.** Merger of 2 or more companies into one new company.
- **Name Change.** Name changes are normally proposed and approved at the company's shareholders' meeting. This has no effect on the capital and shareholders of the company.
- **Par Value Change.** Similar to stock splits where the share nominal value is changed which results in a change in the number of shares held.

- **Scheme of Arrangement.** Scheme of Arrangement occurs when a parent company takes over its subsidiaries and distributes proceeds to its shareholders.
- **Scrip Dividend.** (The UK version of an optional dividend). The shareholder can elect to receive either cash or new shares based on the ratio. The default is usually cash.
- **Scrip Issue.** Shareholders are awarded additional securities (shares, rights or warrants) free of payment. The nominal value of shares does not change
- **Spin-off.** A distribution of subsidiary stock to the shareholders of the parent corporation without having cost to the shareholder of the parent issue.
- **Stock Dividend.** Almost identical to bonus issues where additional shares are issued to shareholders.
- **Stock Split.** A company can decide to increase the amount of its outstanding shares while at the same time decreasing the market share price.
- **Return of Capital.** A cash amount will be paid to investors in combination with a nominal value change of the shares.
- **Reverse Stock Split.** A company can decide to decrease the amount of its outstanding shares while at the same time increasing the nominal share price.
- **Cash Stock Option.** Shareholders are offered the choice to receive the dividend in cash or in additional new shares of the company.
- **Merger with Elections.** Merger of two or more companies into one new company. The shares of the old companies are consequently exchanged into shares in the new company according to a set ratio.
- **Spin-off with elections.** A distribution of subsidiary stock to the shareholders of the parent corporation without having cost to the shareholder of the parent issue whereby the shareholders are offered choices regarding the resultant stock.
- **AGM/EGM – proxy voting.** Every publicly traded company has an annual general meeting where management presents several decisions that need shareholder approval. The approval is given by means of voting for or against each decision. Shareholders may attend the meeting in person or vote by proxy.
- **Buy-back program/Repurchase Offer.** Offer by the issuing company to existing shareholders to repurchase the company's own shares or other securities convertible into shares. This results in a reduction in the number of outstanding shares.
- **Dividend Reinvestment Plan.** The company pays the cash dividend after which shareholders are offered the possibility to reinvest the cash dividend in new shares.
- **Dutch Auction.** A Dutch Auction offer specifies a price range within which a fixed number of shares will ultimately be purchased. Shareholders are asked to submit instructions as to what price they are willing to sell. Once all instructions have been counted, the shares of the shareholders who voted to sell at the lowest prices will be bought until either the fixed number of shares is reached or the upper limit of the price range is reached.
- **Odd lot Tender.** If the lot is 100 and a shareholder holds 150 shares, an odd lot tender will give the shareholder to dispose of 50 shares at a given price.

- **Rights Auction.** Rights to buy new shares are being auctioned - shareholders who submit the highest prices at which they are willing to buy new shares will get the new shares.
- **Rights Issue.** Rights Issue allows the rights holder to subscribe to additional shares of either the same stock or another stock or convertible bond, at the predetermined rate/ratio and price.
- **Subscription Offer.** Offer to existing shareholders to subscribe to new stock or convertible bonds.
- **Takeover.** One company taking control over another company by acquiring the majority of outstanding share voting rights.
- **Tender Offer.** Offer to purchase a certain number of shares of a company at a given price.
- **Voluntary Exchange / Optional Conversion.** Offer to exchange shares into cash or other shares.
- **Conversion of convertible bonds.** Convertible bonds are being converted in the underlying shares
- **Interest payment/Coupon Payment.** The issuer of the bond pays interest according to the terms and conditions of the bond.
- **Early Redemption.** The issuer of the bond repays the nominal, with accrued interest, prior to the maturity date of the bond.
- **Lottery, a/k/a drawing.** The issuer redeems selected holdings before the maturity date of the bond (early redemption).
- **Partial Redemption.** The issuer of the bond repays part of the nominal, with accrued interest, prior to maturity.
- **Final Redemption.** The issuer of the bond repays the nominal of the bond, with accrued interest.

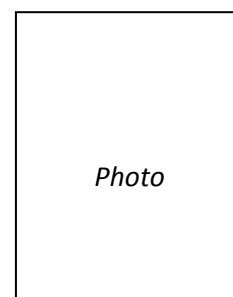
Annex of Joint resolution no 85/A-106 of  
Chairman of Financial Regulatory Commission  
and Governor of Mongolbank on July 3<sup>rd</sup>, 2014

**Annex II of the Regulation on Custodian Licensing and Custodian Services**

**Information on the chief executive of the Custodian or manager of the Custodian Custody Operations Unit**

1. The below form shall be accurately completed and submitted by the chief executive, manager or other personnel of the regulated entity:

- Full name:
- Position/title:
- Date of birth:
- Nationality:
- Home address:
- Telephone:
- Passport number:
- Current job:
  - duration:
  - address:
- Education /please include the middle education /



No.	School	Vocation	Year of enrollment	Year of graduation	Number of diploma/certificate

- Work experience:

No.	Employer	Position/title	Date of commencement of employment	Date of termination of employment	Reason [of termination]

- Details on executive management and personnel (including, without limitation, if they represent a legal person, core activities of the legal person, location, history of dealing with regulated entity(ies), correspondent banks, shareholding in a legal person, debts and other outstanding liabilities to 3<sup>rd</sup> parties, any criminal proceedings etc.).

2. Legal status of the executive management and personnel:

For definition of “affiliated persons”, please refer to Article 99 of the Company Law.

No.	Nature of affiliation	Full name	Passport number	Position/title

*Please describe previous work history, affiliation with legal persons, core activities of the legal person, location, debts and other outstanding liabilities to 3<sup>rd</sup> parties, any criminal proceedings etc. in respect of affiliated persons.*

*Please also enclose statements from law enforcement, tax, bank and applicable institutions and individuals in respect of the executive management or personnel.*

On behalf of . . . . .

/title/

/ . . . . . /

/signature/

/ . . . . . /

/full name/